



PHILIP MORRIS

REFERENCE MANUAL
FEDERAL REGULATIONS
BUREAU OF ALCOHOL, TOBACCO AND FIREARMS

General Accounting Department
November 1983

PM3000760871

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INTRODUCTION

The taxation of tobacco, as imposed by the Federal government under the jurisdiction of the Bureau of Alcohol, Tobacco and Firearms, (ATF), is divided into four categories: cigarettes, cigarette papers, cigarette tubes and cigars.

The purpose of this manual is to outline aspects of federal regulations regarding not only the taxation requirements for cigarette manufacturers, but also to provide some insight into regulatory restrictions imposed by the government concerning the operations of a tobacco facility.

It is not the intention of this guide to be the only source of information, nor is it intended to replace those internal procedures currently in place that are within the guidelines of the federal regulations. It is intended to provide a base of information for reference.

The Revenue Accounting department, located in the Finance Center, is responsible for all correspondence with ATF concerning regulatory compliance. This department is to be considered the source for information concerning questions relative to compliance or operational requirements.

Failure to comply with Federal regulations governing the operations and reporting requirements imposed against a tobacco facility may result in the assessment of fines or penalties. Tobacco permits are issued by the government based on the manufacturer's assurances that operations will be conducted in the manner prescribed by law. Permits can be withdrawn at any time, if irregularities are disclosed.

PM3000760873

FOREWORD

Tobacco permits are issued by the Bureau of Alcohol, Tobacco and Firearms under the authorization of the Federal Government.

Currently, Philip Morris holds the following valid tobacco permits:

TP-7-VA	Richmond, Virginia
TP-24-KY	Louisville, Kentucky
TP-625-NC	Cabarrus-Concord, North Carolina
TP-13-VA	Williamsburg, Virginia (York Eng.)

Only these facilities and those locations included under their respective permits are considered to be part of the manufacturer's factory premises. As part of the factory premises, the facilities are considered to be bonded locations. This status allows for the manufacture, receipt, distribution and storage of cigarettes without payment of federal excise taxes in certain instances.

A listing of all bonded locations covered by the Richmond permit can be found at the end of this guide.

The tax rates on cigarettes are determined by categories:

Class A: Termed small cigarettes and are taxed at \$8.00 per thousand and weigh not more than three pounds per thousand cigarettes.

Class B: Termed large cigarettes and are taxed at \$16.80 per thousand and weigh more than three pounds per thousand cigarettes.

Currently, all cigarettes of Philip Morris manufacture are Class A cigarettes.

Tax liabilities are established when cigarettes are produced, received in bond, or returned to bond. Briefly, any addition to the inventory of cigarettes on bonded premises increases the expressed tax liability.

Additionally, tax liabilities are incurred as a result of the following:

- any shortage discovered as a result of a physical inventory.
- the distribution or use of cigarettes in a manner not authorized by Federal regulations.

- any loss of cigarettes in transit which are traveling in bond from the premises of one bonded facility to the premises of a second bonded facility.
- any loss or shortage of cigarettes diverted from shipments destined for exportation.

Tax payments are determined at the time the cigarettes are removed from bonded premises or discrepancies as noted above are disclosed. Tax payments are based on fifteen day removal periods and are paid by return filed with the Internal Revenue Service.

As the federal agency charged with the responsibility of enforcing regulatory requirements, ATF issues regulations relative to the business operations of all tobacco manufacturers. Regulations pertain not only to the production and shipment of cigarettes, but are also relative to the following areas:

- receipts of cigarettes into bonded inventories
- reduction of cigarettes to tobacco
- destruction of cigarettes
- experimental/sample use of cigarettes
- cigarette packaging requirements
- physical inventories of finished goods on bonded premises

During the operating hours of any tobacco manufacturing facility, any ATF officer may enter the bonded premises where cigarettes are produced or kept for the purpose of examining such products. The owner of such premises, or the person having superintendence of same, who refuses entry or examination, is liable to penalties and fines as prescribed by law.

It is advisable for each bonded location to have written procedures to be followed during any inspection visit by ATF. Copies of in-house procedures for each location should be on file with Revenue Accounting and should list the employees at that location who will be in direct contact with the inspectors. Revenue Accounting should be advised when an ATF officer is on premise. It is Philip Morris policy to escort ATF agents through facilities for purposes of safety and security. No documents, cigarettes, or cigarette materials should be supplied to ATF inspectors during any visit. All requests should be routed through Revenue Accounting, who will in turn provide the ATF inspectors with the requested information or materials.

Every manufacturer of tobacco products is required by federal law to keep records of his operations and transactions for each day. All recording of this information must accurately reflect operations for the day of occurrence. The records shall show by date and quantity, cigarettes that are:

- manufactured
- received in bond by:
 - transfer from other factories
 - release from customs custody
 - transfer from export warehouse
- received by return to bond
- disclosed as an overage by physical inventory
- removed - subject to tax
- removed in bond for:
 - export
 - transfer to export warehouse
 - transfer to other factories
 - use of United States
 - experimental purposes off factory premises
- otherwise disposed of, without determination of tax, by:
 - consumption by employees off factory premises
 - use for experimental purposes off factory premises
 - loss
 - destruction
 - reduction to tobacco
 - disclosed as a shortage by physical inventory

Additionally, records must be kept for cigarettes on which the taxes have been determined (reported or paid), and which are:

- received
- disposed of

All records required to be maintained as supporting documents to substantiate the operations of the manufacturer must be retained for three years following the close of the calendar year in which the operation is concluded.

Various operations of a manufacturer of tobacco products require special authorizations from the federal government. This would include, but may not be limited to:

- the destruction of cigarettes that are part of the bonded inventory
- the shipment of loose or packed cigarettes from PM's bonded premises to an outside concern that does not have a tobacco permit
- the exportation of loose cigarettes
- the addition or deletion of a facility or portions of a facility in relation to PM's tobacco permit
- any variations from ATF approved packaging requirements
- the return of cigarettes to PM that were previously reported as removals from inventory
- the destruction of cigarettes removed as tax determined, that are returned to the manufacturer for credit

It is the responsibility of the originator of any transaction that requires special ATF authorization to contact Revenue Accounting, in writing, with details of the proposed project. Revenue Accounting will then contact ATF and submit the necessary applications for approval. Ample time must be allowed to obtain approvals. Any questions concerning special authorizations must be directed to Revenue Accounting.

OPERATIONS AND REPORTING REQUIREMENTS

<u>Operation</u>	<u>P. M. Requirements</u>	<u>ATF Requirements</u>
<u>Manufacturing</u>	Daily production reports for domestic, export and sample/experimental production. Must reflect verified quantities for opening inventory, production, transfers in, transfers out, closing inventory, reduced to tobacco and where applicable, destruction and inventory discrepancies.	Accurate reflection of the day's transactions for the day of occurrence.
<hr/>		
<u>Receipts Into Factory</u>		
Previously Tax Determined Cigarettes Returned from Market	Routed through the Returned Goods department. Labeled as 'TPD' (Tax Previously Determined). Internal documentation of receipt forwarded to General Acctg. for preparation of ATF application forms. Addition to inventory recorded on day of occurrence.	ATF approval required for disposition via Form 3069 submitted by Accounting. No disposition until approval is received from ATF.
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<u>In-Bond Receipts</u>		
Transfers from the bonded inventory of another manufacturer of TP products. (Includes PM and any other permit holder)	Generally reported by Finished Goods. Reflected on daily reports as increase to inventory. Internal documentation to reflect identity of sender to allow for future audit of receipts by ATF or PM personnel.	No special authorization from ATF required. Considered to be in-bond transfer. Adequate recordkeeping required.

OPERATIONS AND REPORTING REQUIREMENTS

<u>Operation</u>	<u>P. M. Requirements</u>	<u>ATF Requirements</u>
Transfers from the inventory of an export warehouse	Routed through Returned Goods department. Internal documentation of receipt reflecting all pertinent information. PM must be in receipt of ATF Form 2149/2150 issued by sender.	No special authorization. Completed ATF Form 2149/2150 must be available for ATF audit of returns.
Export cigarettes returned to PM prior to exportation	Routed through Returned Goods department. Internal documentation of receipt reflecting all pertinent information. PM must be in receipt of ATF approved Form 2149 which allows return of cigarettes to inventory.	ATF approval required on duplicate copy of Form 2149 - original shipping document. No disposition until approval is received.
Cigarettes exported and later returned to PM (Includes Imported Cigarettes)	Routed through Returned Goods department. Internal documentation of receipt reflecting all pertinent information. PM must be in receipt of certified ATF Form 2145 before returning cigarettes to inventory.	ATF and U.S. Customs certified Form 2145 approving release of cigarettes to manufacturer required for disposition.
Factory Smokes Returned from inventory location (Tax Paid or Tax Free)	Routed through Returned Goods department. Properly marked as to tax classification. Internal documentation of receipt forwarded to General Accounting for preparation of ATF application forms. No disposition until approval is received.	ATF approval required for disposition via Form 3069 submitted by Accounting.

OPERATIONS AND REPORTING REQUIREMENTS

<u>Operation</u>	<u>P. M. Requirements</u>	<u>ATF Requirements</u>
Unclaimed Goods (Domestic or Export)	Routed through Returned Goods department. Internal documentation of receipt forwarded to General or Revenue Accounting for preparation of ATF applications for approval as necessary.	ATF approval required for disposition of domestic returns via Form 3069. Export returns are recorded via internal tallies and returned to stock without ATF approval.
<hr/>		
	All applications filed with ATF for permission to return cigarettes to PM's inventory are subject to inspection by ATF agents. Where required, no disposition of cigarettes may be initiated until ATF approval has been received. The return of cigarettes that have been previously tax determined, (either reported or paid) allows PM to claim credit for the taxes. Once disposition of the cigarettes has been completed, all internal documentation is subject to ATF inspection and verification.	
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Reduction of Cigarettes to Tobacco	Reported on daily manufacturing report <u>on the day of occurrence</u> . Entry must reflect kind, quantity and weight of tobacco recovered.	No authorization required. Reporting of weight of recovered tobacco is required by law. It is unlawful to reduce the manufacturing quantity by the amount reduced to material.
<hr/>		
<u>Destruction</u>		
Destruction of Cigarettes Recorded in Manufacturer's Factory Records	Requires written request for ATF permission to destroy to be forwarded to Revenue Acctg. Only Finished Goods, Rework & R&D Semiworks may report destruction. All goods to be destroyed from inventory will be billed by Customer Service. Destruction must be reported on internal documentation on the day of occurrence.	Requires ATF approval prior to disposition. Cigarettes to be destroyed are subject to ATF inspection prior to granting of approval. It is unlawful to destroy cigarettes prior to receipt of authorization from ATF, or prior to actual disposition.

OPERATIONS AND REPORTING REQUIREMENTS

<u>Operation</u>	<u>P. M. Requirements</u>	<u>ATF Requirements</u>
<u>Destruction of Cigarettes Tax Determined - Off Factory Premises</u>	<p>These are cigarettes removed from the factory premises as taxable shipments. When the cigarettes are damaged in the field to such an extent that on-site destruction is necessary, special procedures must be followed.</p> <p>Revenue Accounting must be notified immediately. No disposition of the cigarettes may take place, regardless of what information is supplied by any other ATF regional office. PM's ability to reclaim taxes paid is dependent on following procedures required by our ATF regional office.</p>	Requires ATF approval from PM's region prior to any disposition.
<u>Factory Smokes</u>	<p>Storage areas, cabinets and dispensers must be locked at all non-use times. Only personnel responsible for the maintenance of factory smokes inventories should have access to keys.</p> <p>Physical inventories of both tax paid and tax free factory smokes on the last working Friday of <u>every month</u>.</p> <p>Prominent display of signs indicating unlawful acts regarding un-taxed factory smokes and stating both company policy and federal law concerning violators.</p> <p>Notices on dispensers stating the daily allotment allowed and warning against resale or giveaway of the cigarettes.</p>	<p>Provide separation of inventories by tax class. Provide adequate security to inventories. Record all transactions involving factory smokes.</p> <p>Employees in a bonded facility may be furnished one pack of non-taxed cigarettes on each day the employee is at work.</p> <p>Non-taxed cigarettes furnished to the employee must be furnished within the bonded premises and must be removed by the employee on the same day.</p> <p>By federal law, it is unlawful to sell, offer for sale or give away cigarettes furnished to employees for their personal consumption.</p>

OPERATIONS AND REPORTING REQUIREMENTS

Operation

Factory Smokes

P. M. Requirements

Stale date cigarettes or excess inventories must be returned to the Returned Goods department via an Intra-Co transfer form. The transfer form must identify the cigarettes by brand and quantity and must identify the tax classification of the cigarettes. All transactions of this nature must be reported on the weekly factory smokes inventory reports.

Dispensers must be supervised during all hours of distribution.

All receipt and distribution quantities must be verified prior to recording.

ATF Requirements

Non-taxed factory smokes may not be utilized in un-bonded areas.

All transactions must be recorded on the day of occurrence.

All transactions must be traceable through supporting documents.

Any loss in inventory, theft, overage in inventory, transfer of cigarettes to Returned Goods, shortage in receipt, etc., must be reported and recorded on all internal documents.

Sample Experimental Uses of Cigarettes

From PM Manufacturing Location to PM Testing Facility on Bonded Premises

Recording of production and transfer on the manufacturing report of the sending location. Intra-Co. Transfer form to accompany manufacturing report.

No special authorization required to ship cigarettes between bonded locations. Adequate records to allow for audit of all removals.

From PM Premises to Other Permitted Locations. (Philip Morris or any other bonded manufacturer of tobacco products.)

(packed or loose cigarettes)

Recording of production and transfer on the manufacturing report of the sending location. Intra-Co. transfer form to accompany manufacturing report. Verification of TP number of receiving facility.

No special authorization required to ship cigarettes between permitted locations. Adequate records to allow for audit of all removals.

OPERATIONS AND REPORTING REQUIREMENTS

Operation

From PM to non-permitted facilities for testing.

Domestic shipments of either packed or loose cigarettes.

P. M. Requirements

Written request must be forwarded to Revenue Accounting in order to initiate letter application to ATF. No disposition of cigarettes until approval is received. Recording of production and transfer on the manufacturing report of the sending location. Intra-Co. transfer form to accompany manufacturing report.

ATF Requirements

Approval of special letter of application which states quantity of cigarettes, identity of receiver and the purpose of the test. No disposition of cigarettes allowed until formal approval is granted.

Sample shipments to New York PM Office

All removals of this type are produced and transferred as tax paid samples. The New York office is NOT a bonded facility.

No special authorization required for taxable shipments. Adequate record keeping required to substantiate tax returns.

From PM to an Export destination for testing purposes (Loose cigarettes)

Written request must be forwarded to Revenue Accounting in order to initiate letter application to ATF. Application must be filed with Bureau in D.C. Ample lead time is required. There are no verbal permissions granted by ATF. Recording of production and transfer on the manufacturing report of the sending location. Originator of the request is required to supply Revenue Accounting with the Export Order number and the 2149 Form serial number issued by Finished Goods for the shipment.

Approval of special letter of application which states quantity of cigarettes, identity of receiver and the purpose of the test. No disposition of cigarettes allowed until formal approval is received from ATF.

Adequate recordkeeping to allow for ATF audit of production and shipment.

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OPERATIONS AND REPORTING REQUIREMENTS

Operation

Experimental Cigarettes to be removed from PM in packaging that varies from ATF requirements.

P. M. Requirements

Written request must be forwarded to Revenue Accounting in order to initiate letter application to ATF. Application must be filed with Bureau in D.C. Ample lead time is required. Where possible, sample of alternate packaging should be provided to Revenue Accounting for submission with letter of application.

ATF Requirements

Approval of special letter of application which states quantity of cigarettes to be removed, identify of receiver, purpose of using alternate packaging materials. No disposition of cigarettes allowed until formal approval is received from ATF.

Physical Inventories

Notification to Revenue Accounting of the results of any physical inventory. Notice must be by memo and must show discrepancies by brand. Revenue Accounting will record any discrepancies and file necessary reports with government.

Inventory adjustments will be billed by Customer Service based on the information supplied to Revenue Accounting.

Physical inventories are required at the start and close of operations of a tobacco manufacturer.

Whenever an inventory is conducted, the results of such inventory MUST be recorded in the records of the manufacturer.

An inventory shortage requires payment of federal excise taxes.

An inventory overage increases the expressed tax liability of the manufacturer.

OPERATIONS AND REPORTING REQUIREMENTS

Operation

P. M. Requirements

ATF Requirements

MISCELLANEOUS

- All special applications submitted to Revenue Accounting must be in memo form. To insure proper transfer of information regarding special projects to ATF, no verbal requests will be accepted.
- When it is necessary to transfer loose cigarettes between bonded Richmond locations for packaging, the reporting of production will be done by the location packaging the cigarettes.
- When it is necessary to transfer loose cigarettes between the bonded facilities of the Richmond factories and the bonded facilities of other PM permitted locations, the production quantities will be reported by the Richmond manufacturing facilities and reported as a transfer to the receiving location via an Intra-Co. Transfer form. This form must be submitted to Cost Accounting along with daily production reports.

PACKAGING MARKS AND REQUIREMENTS

All cigarettes, prior to removal for either domestic or export purposes, shall be put in packages of construction that will securely contain the products and that will maintain the marks and notices required by law.

No package of cigarettes shall have contained therein, attached thereto, stamped, marked, written or printed thereon:

- any coupon or other device purported to be or representative of a ticket, chance, share or an interest in or dependent on, the event of a lottery
- any indecent or immoral picture, print or representation
- any statement or indication that United States tax has been paid

Every package must have imprinted thereon, or on a label securely affixed, a mark to consist of:

- the name of the manufacturer removing the product
- the location, by city and state, of the factory from which the cigarettes have been removed

or

- the mark may consist of the permit number of the factory from which the cigarettes are removed.

Under an approved alternate procedure, Philip Morris is allowed to use packaging material for all locations, e.g., Richmond, Louisville and Cabarrus that utilizes a standard address line. That is, all packaging reflects either of the following:

Benson & Hedges
Richmond, VA

or

Philip Morris Inc.
Richmond, VA

Approval for this alternate method of providing the necessary marks was granted to Philip Morris because the identity of the factory where the cigarettes were packaged is provided by imprinting a code letter on the inner foil of all packages. The identifying code letters are:

- V - Richmond, Virginia
- K - Louisville, Kentucky
- N - Cabarrus, Concord, North Carolina

The imprinting of these identification codes is a matter of record with ATF and must appear on all cigarette packages of Philip Morris manufacture. Failure to comply with this approved alternate method could result not only in fines, penalties and assessable interest charges, but could also result in the loss of the approved alternate procedure. This would mean that Philip Morris would have to provide specific packaging material for each location that would reflect each individual address. Inventories of materials could not be interchanged between locations.

Every pack of domestic cigarettes must have the following either imprinted on or on a label securely affixed, the following:

- the designation, "cigarettes"
- the quantity of the products contained therein
- the classification, i.e.,
 - for small cigarettes, either "small" or "Class A"
 - for large cigarettes, either "large" or "Class B"

Every package of cigarettes removed from the factory for export purposes, must have adequately imprinted thereon, or on a label securely affixed, the words,

"TAX EXEMPT FOR USE OUTSIDE U.S." or "U.S. TAX EXEMPT"

The only exception is where a stamp, sticker or notice that is required by a foreign country or possession of the U.S. readily identifies the product as export. Evidence of this requirement must be maintained at the factory (Revenue Accounting), and be readily available for inspection by ATF agents at their discretion.

The tax exempt notice must be printed in type equivalent to 6-point New Gothic Bold caps on a contrasting background, separate and apart from other descriptive statements.

Every shipping case used for export cigarettes, or any other container in which cigarettes are to be removed for exportation must bear a distinguishing number which as been assigned by the manufacturer.

BONDED LOCATIONS

Richmond Facilities

<u>ADDRESS</u>	<u>LOCATION</u>
4001 Commerce Road	Finance Center
1915 E. Main Street	20th Street Plant
700 Stockton Street	Stockton Street Plant
4201 Commerce Road	R&D Facility
2325 Maury Street	Stemmery
2211 Bells Road	Finished Goods Domestic Whse.
2200 Bells Road	Flavoring Center
121 South 15th Street	Dock Street
2301 Everett Street	B&L Plant
4101 Commerce Road	Old Engineering/Now R&D
300 Commerce Road	Westab Building
5612 Biggs Road	Training Center
3601 Commerce Road	Manufacturing Center/Primary East Wing/Finished Goods
2900 Cofer Road (and Cooler #4)	Munford Cold Storage
4200 Deepwater Terminal Road	James River Center-14 Bldgs.
2326 Bells Road	Returned Goods Department
700/702 Everett Street	Westab Annex
1820 West 100 Road	Richmond Cold Storage
709 Stockton Street	Stockton Street Machine Repair
2303-2305 Bells Road	South Warehouse
2001 Walmsley-Bldg. I,II, III and Q.A.	Operations Center